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IN THE

Supreme Court of the United States

OCTOBER TERM, 1970

CONTINENTAL CAN COMPANY, INC., PETITIONER

v.

THE UNITED STATES

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

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The petitioner, by its counsel, petitions for a Writ of Certiorari to review the judgment of the United States Court of Claims in this case.

Opinion Below

The opinion of the Court of Claims (App., *infra*, pp. A 1-A 40) is reported at 422 F. 2d 405.

Jurisdiction

The judgment of the Court of Claims was entered on February 20, 1970 (App., *infra*, pp. A 1, A 56). The jurisdiction of this Court is invoked under 28 U. S. C. 1255(1).

Questions Presented

Under the compulsion of an antitrust decree and under the close supervision and control of the Federal Court petitioner sold used can closing equipment at a gain. The machinery had been held solely for lease to purchasers of cans manufactured by the petitioner, and at the beginning of 1951 had been held for an average of more than 16 years. The machinery in question was sold to lessees who were in possession of it at the date of the decree at prices fixed by the Court. These prices were below market value. Petitioner realized a profit as a result of the fact the machinery was heavily depreciated.

The petitioner is entitled to report profit from such sales for Federal income tax purposes as capital gains rather than as ordinary income, unless the property sold was "held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business," within the meaning of Section 117(j) of the 1939 Code (now Section 1231 of the 1954 Code). The proper application of the quoted language raises three questions presented for review in this case:

1. In determining whether property was held primarily for sale, and thus deprived of the tax treatment normally afforded dispositions of property used in the taxpayer's business, is the result controlled by the taxpayer's purpose at the time of sale, as the Court of Claims held, or must it be determined from the circumstances of the entire period during which the property was acquired, held, and used, as the petitioner maintains.

2. Whether court forced sales of property, supervised by a special master, at prices below fair market value and upon terms fixed by a court decree are sales to customers in the ordinary course of business within the meaning of the income statute.

3. Has the Court of Claims applied the proper legal standard in ruling that property was held "primarily" for

sale within the meaning of the governing statute simply because the property was regularly offered for sale as a result of the antitrust decree?

Statute Involved

Internal Revenue Code of 1939:

SEC. 117 [as amended by Sec. 151(b), Revenue Act of 1942, c. 619, 56 Stat. 798, and Sec. 210(b), Revenue Act of 1950, c. 994, 64 Stat. 906] CAPITAL GAINS AND LOSSES.

(j) *Gains and Losses from Involuntary Conversion and from the Sale or Exchange of Certain Property Used in the Trade or Business.*—

(1) *Definition of property used in the trade or business.*—For the purposes of this subsection, the term "property used in the trade or business" means property used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23(l), held for more than 6 months, and real property used in the trade or business, held more than 6 months, which is not (A) property of a kind which would properly be includible in the inventory of the taxpayer if on hand at the close of the taxable year, or (B) property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or (C) a copyright, a literary, musical or artistic composition, or similar property, held by a taxpayer described in subsection (a)(1)(C).

(26 U. S. C. 1952 ed., Sec. 117).

Statement

The petitioner, Continental Can Company, Inc. (Continental), is, and in 1951 was, a manufacturer of metal containers. Finishing the containers by fixing tops to them,

after filling, was done with machinery which Continental leased to its packer customers. With immaterial exceptions, Continental never sold can closing machinery (Findings 6-8, 10, App., *infra*, pp. A 41-42.)[1]

Under the compulsion of a decree of the Federal District Court for the Northern District of California, Continental was obliged to end its former leasing practice by January 1, 1951. It was required to offer can closing machinery and related equipment ("closing machinery") for sale or lease, according to the wishes of the customer. This case involves closing machinery in the hands of lessees on January 1, 1951 and which was sold to such lessees pursuant to the decree (Findings 12-13, 16, 18, App., *infra*, pp. A 43, A 44, A 45).

The decree required that closing machinery manufactured or acquired by Continental prior to 1951 be offered for sale to lessees then in possession of the equipment at court-decreed formula prices which were under fair market value and actually below replacement cost. Lessees were given an absolute priority to buy the machinery at the decree prices or to continue to lease the machinery indefinitely. A special master appointed by the court closely supervised the sales of closing machines (Findings 20, 22, 28-30, 33, App., *infra*, pp. A 46-47, A 48, A 49-A 50, A 51). If a lessee in possession elected to purchase the closing machinery at the decree price, petitioner was not permitted to sell to another purchaser who offered a higher price. Moreover, petitioner could not sell the machinery to anyone if the lessee elected to continue to rent the machinery in his possession. Thus, the decree designated the offerees of the property, namely, lessees in possession, the terms of sale, and made petitioner subject to strict compliance with the decree through the policing of a special master.[2]

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[1] It made only isolated sales to the Government or to its foreign subsidiaries (Finding 10, App., *infra*, p. A 42).

[2] See Findings 28-30, App., *infra*, pp. A 49-A 50, as to the special master.

The machines sold to lessees in possession had been held solely for leasing for an average of 16.6 years and in some cases for an average of 30 years. The 1951 sales produced a taxable gain of $1,720,639 which was reported as capital gain under Section 117(j) of the Internal Revenue Code of 1939, which provides such treatment for depreciable property used in the taxpayer's business. The Commissioner of Internal Revenue held that these sales were excluded from the benefit of Section 117(j) on the ground that the property had been held primarily for sale to customers in the ordinary course of business (Findings 31, 44, App., *infra*, pp. A 50, A 54).[3] The Court of Claims, dividing four to three, adopted the decision of its Trial Commissioner against the petitioner.

Reasons for Granting the Writ

1. A taxpayer who sells at a profit depreciable property used in his business is taxed at capital gains rates unless the property was held primarily for sale to customers in the ordinary course of business. In determining whether the sale of closing machinery was within the general rule or the exception, the Court of Claims has insisted on determining the taxpayer's purpose from the circumstances at the moment of sale rather than during the full period from acquisition to sale. The Court of Claims' holding is in error and is in direct conflict with The Third Circuit in *Philber Equipment Corp.* v. *Commissioner*, 237 F. 2d 129.

Philber dealt with sales of trucks by a rental company and the Third Circuit held that gain from the sales did not result in ordinary income. The Court said (237 F. 2d at 131-132):

> We are here concerned with a going operation which involves continuous rental, purchase and sale, and

[3] For that reason, the gain was not only taxed as ordinary income but also included in excess profits tax net income (Finding 44, App.; *infra*, p. A 54).

> the *determinative factor is the purpose for which the property was held at the time of its acquisition and during the period of its use.* [Citations omitted.] The final sale of the property can only be decisive if the taxpayer's business was operated with the final gains from the sale of the vehicles as a determining business purpose. We think the record supports the taxpayer's contention that the acquisition, use and disposition of its equipment was consistent with the business purpose of vehicle rental and not vehicle sale. [Emphasis added.]

To the same effect, see *United States* v. *Bennett*, 186 F. 2d 407 (5th Cir.); *McGah* v. *Commissioner*, 193 F. 2d 662, 663 (9th Cir.); *Municipal Bond Corp.* v. *Commissioner*, 341 F. 2d 683, 689 (8th Cir.).[4]

There is no dispute as to the relevant facts here. Before January 1, 1951, the closing machinery sold was held exclusively for use in Continental's business and not for sale to customers. Thereafter, as a result of the 1951 antitrust decree, this machinery became subject to purchase by the lessee at his option. The Court's decision in this case shuts its eyes to the purpose for which the property was acquired and held for up to thirty years prior to 1951 and looks only to the fact that the machines were sold as proof that they were held primarily for sale. If this were a correct interpretation of the law, the legislative purpose would be totally subverted since at the time of sale all property is held primarily for sale.

In dismissing the taxpayer's purpose during the lengthy holding period before the sale, the Court of Claims is in conflict with the underlying theory of the capital gains provision. In *Malat* v. *Riddell*, 383 U. S. 569, 572, this Court stated that the "primarily" test differentiates between the profits and losses arising from the everyday

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[4] The Court of Appeals in *Municipal Bond Corp., supra*, at 689 stated: "we emphasize that the Tax Court in making its findings should not limit its consideration solely to circumstances existing at the time of sale."

operation of a business on the one hand and the realization of appreciation in value accrued over a substantial period of time on the other. Quite clearly, the Court of Claims, by narrowly restricting its attention to purpose at the moment of sale, ignores that long period of time over which the gain here in issue accrued and has virtually sterilized the statute.

2. Since petitioner did not hold closing machines for sale before the antitrust decree, the decision of the Court of Claims is incorrect on grounds independent of its ruling as to the time for determining purpose if, as we contend, the sales to lessees were not made in the ordinary course of Continental's business.

Continental's principal business was and is the manufacture and sale of containers, not machinery. The property here in issue was disposed of to lessees selected by a Federal Court at abnormally low prices determined by that Court, on terms and conditions promulgated by the Court and under the supervision of an officer of the Court. This involuntary mode of selling what had been Continental's productive machinery, the Court of Claims held, constituted the ordinary course of petitioner's business. This extraordinary interpretation of the word "ordinary" is attempted to be justified by the Court of Claims in two ways. First, it states that since the antitrust proceeding was concluded by a "consent" decree that Continental willingly signed, such willingness makes the resulting conduct "ordinary" without regard to its actual character.[5] The reasoning is plainly unsound. There can be no warrant whatever in

[5] Petitioner had stipulated to a suspension of proceedings in the antitrust suit pending the final decision in an antitrust suit that the Government had instituted against American Can Company. Petitioner had further consented to entry of a decree in its case in substantially the same terms as might be entered as to the American Can Company unless the decree required divestiture of petitioner's entire can closing operations (Finding 15, App., *infra*, p. A 43-A 44). The decree in question was entered pursuant to the stipulation.

holding that an antitrust consent decree reflects a voluntary choice. It is true that petitioner, facing the possibility that it might be required to divest itself of its entire can closing operation, elected to sign the consent decree rather than to risk a more drastic result. But in no rational sense did this represent a choice that petitioner would have made in the absence of the compulsion of an antitrust suit. And if it were realistic to treat this type of consent as a voluntary choice, this factor still would not have any logical bearing on whether the decreed course of conduct was "ordinary"—that is, usual, common or regular—as the statute clearly requires. The Court of Claims' holding that the petitioner's collaboration by its consent to the decree turned the resulting course of conduct into the ordinary course of business, does violence to the plain English of the statute and should not be sustained.

Second, the Court of Claims has equated sales under this decree to the administrative supervision of various classes of regulated industry. But we are dealing here with a short-term, finite program involving the sales of a specific class of property to a specified group (lessees) at court-determined prices and under specific supervision, all of which came to an end when it was done. This is in no way similar to the continuous and uniformly applied public interest regulation of utilities, meat packers and securities dealers. And, indeed, such industries are not required, as an ordinary aspect of their regulated businesses, to divest themselves of productive machinery at prices below replacement cost. The decree in the antitrust litigation brought against Continental provided for what can only be regarded as an extraordinary course of conduct for any business.

3. The Court of Claims has failed to follow *Malat* v. *Riddell*, 383 U. S. 569.

The *Malat* case, of course, held that the "primarily for sale" language was to be accorded a "literal reading"—"'of first importance' or 'principally'." 383 U. S. at 572.

Disregarding that legal standard, the majority of the Court of Claims here adopted the view that "where a company is, at such date [the date of sale], regularly engaged in the dual business of selling and renting its machines, then income resulting from either activity satisfies the 'primarily' concept" (App., *infra*, p. A 10). This notion of regularity of sales was introduced by the Court of Claims prior to *Malat* in *Recordak Corp.* v. *United States*, 163 Ct. Cl. 294, 325 F. 2d 460. The dissenting opinion of Judge Skelton in the present case, joined by two other judges of the Court of Claims, correctly explains that this reading of the statute "does not meet the requirements of the Supreme Court's definition" (App., *infra*, p. A 32):

> The word "regularly" has about the same meaning as "substantially" which was erroneously used in *American Can* [317 F. 2d 604 (2d Cir. 1963), *certiorari denied*, 375 U. S. 993 (1964)] to define "primarily." Goods could be "regularly" offered for sale without being "principally" offered for sale and without sale being the object of "first importance" in the offering. They could be offered "principally" for lease and with rentals being of "first importance", even though "regularly" offered for sale. In such case, under the Supreme Court's definition, the goods would not be held "primarily" for sale, and any gain by the taxpayer on their sale would be long term capital gain under Section 117(j) of the Code.

The majority of the Court of Claims appears to be firmly convinced that the non-literal definition of "primarily" enunciated in *Recordak* is sound simply because this Court's *Malat* decision, in listing the conflicting lower court cases, referred to *Recordak*, with a "Cf." citation (383 U. S. at 571, note 3). We submit that this citation which followed the list of cases that had *distinctly* taken the erroneous view that "primarily" meant "substantially", was intended to suggest that *Recordak* fell within the same category, *i.e.*, the group of cases in which "primarily" was accorded a non-literal interpretation. It would appear that the

prefatory "Cf." merely denoted that *Recordak* had not precisely stated that "primarily" and "substantially" were equivalent, but had chosen a similar incorrect interpretation based on regularity.[6] In sum, we believe that a fair construction of this Court's *Malat* holding requires the conclusion that the *Recordak* theory which the Court of Claims applied here was plainly overturned.

The Court of Claims' persistence in an unsound standard is further demonstrated, as the dissenting opinion points out (App., *infra*, p. A 31), by the majority's heavy reliance on *American Can Co.* v. *Commissioner*, 317 F. 2d 604 (2d Cir.), *certiorari denied*, 375 U. S. 993, one of the cases which this Court noted in *Malat*, had accepted the improper "substantially" standard. At a minimum, *Malat* completely neutralized *American Can* as a precedent and the petitioner was entitled to have its case decided without regard to the result reached by the Second Circuit on an improper basis.[7]

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[6] Point A of the Government's brief (p. 12) in *Malat* made the argument, rejected by this Court, that a taxpayer holding property for the dual purpose of rental or sale is perforce not "entitled to have his *regular* business profits from its sale taxed as capital gains" (emphasis added). The Government's *Malat* brief (pp. 10, 20, 21, 22) frequently cited *Recordak* among the cases adopting its position and specifically discussed it at length in support of its argument.

[7] The Court of Claims' approach was, moreover, out of keeping with the procedure followed by this Court in *Malat* (383 U. S. at 572): "Since the courts below applied an incorrect legal standard, we do not consider whether the result would be supportable on the facts of this case had the correct one been applied. We believe, moreover, that the appropriate disposition is to remand the case to the District Court for fresh fact-findings, addressed to the statute as we have now construed it." Similarly, the Court of Claims should have paid no heed to *American Can*, but should have considered its own fact-findings, "addressed to the statute as" this Court has "construed it."

Conclusion

For these reasons, we believe that the petition for a writ of certiorari to the United States Court of Claims should be granted.

Respectfully submitted,

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Of Counsel:

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May, 1970.

APPENDIX

IN THE UNITED STATES COURT OF CLAIMS

No. 102-64

(Decided February 20, 1970)

CONTINENTAL CAN COMPANY, INC.

v.

THE UNITED STATES

Robert B. Hodes, for plaintiff. *Thomas N. Tarleau,* attorney of record. *Willkie Farr & Gallagher* and *Nicholas J. Sheppard,* of counsel.

Joseph Kovner, with whom was *Assistant Attorney General Johnnie M. Walters,* for defendant. *Philip R. Miller,* of counsel.

Before COWEN, *Chief Judge,* LARAMORE, DURFEE, DAVIS, COLLINS, SKELTON, and NICHOLS, *Judges.*

OPINION

PER CURIAM: This case was referred to Trial Commissioner Saul Richard Gamer with directions to make findings of fact and recommendation for conclusions of law under the order of reference and Rule 57(a) [since September 1, 1969, Rule 134(h)]. The commissioner has done so in an opinion and report filed on February 27, 1969. Plaintiff filed no exceptions to the commissioner's findings of fact but did except to his opinion and recommended conclusion

of law. Defendant requested adoption of the findings of fact and the recommended conclusion of law. The case has been submitted to the court on the briefs of the parties and oral argument of counsel.

Since the court agrees with the commissioner's opinion, findings and recommended conclusion of law, as hereinafter set forth, it hereby adopts the same as the basis for its judgment in this case.* Therefore, plaintiff is not entitled to recover and the petition is dismissed.

OPINION OF COMMISSIONER

GAMER, *Commissioner:* Plaintiff seeks recovery of over $3,150,000 as claimed overpayments of federal income and excess profits taxes, and interest paid thereon, for plaintiff's calendar year 1951, plus statutory interest.[1]

Plaintiff (hereinafter sometimes referred to as "Continental") has long been a manufacturer of can containers for food, beverages, and other products.

For over 35 years prior to January 1, 1951 (*i.e.*, ever since its incorporation in 1913), plaintiff, as an incident of the sale of cans to its customers (canners), installed in their plants certain equipment which effected proper closure of the cans. During that period, plaintiff leased the equipment to its customers at nominal rentals under an arrangement, however, whereby the user of the equipment was obliged to purchase its can requirements from plaintiff.

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* The dissenting opinion of SKELTON, *Judge*, in which COLLINS, *Judge*, and NICHOLS, *Judge*, join, follows the opinion of the trial commissioner which has been adopted by the court.

[1] The petitions filed by plaintiff in Case Nos. 130-67 and 131-67, claiming $1,264,630 and $751,779, respectively, with respect to 1952 and 1953, involve the same issues as the instant claim. Proceedings in such two cases have been suspended pending the disposition of this case.

Plaintiff leased the equipment only to its container customers. Plaintiff's can-closing machines were not held for sale and (except for a few isolated and immaterial instances) were not sold.

In August 1946, the Government instituted an action in the District Court for the Northern District of California against Continental for alleged violation of the Sherman and Clayton Acts. The action was in part based upon Continental's restricted sales policy and its practice of tying the sale of containers into the leasing of the closing equipment. The Government sought either (a) divestiture of the closing-machine part of Continental's business, or (b) a judgment declaring Continental's arrangement with its customers to be illegal and requiring it to either sell or lease its closing machines to any applicant on nondiscriminatory terms.

The American Can Company, the country's largest manufacturer of food and beverage containers (Continental being the next largest) had engaged in substantially the same practices. At the same time that the Government instituted its action against Continental, it also brought a similar action in the same court against American Can.

In September 1949, the Government and Continental entered into a stipulation whereby further proceedings in Continental's case were suspended pending a final decision in the *American Can* case. Continental agreed that, if a decree would be entered against American Can in its case, a similar decree could be entered against Continental at the same time, with the proviso, however, that Continental's decree would contain no provision requiring divestiture of the closing machine portion of its business even though American Can would be ordered to divest. If American Can were ordered to divest, Continental was left free to litigate such question in its case.

On November 10, 1949, American Can's activities were found to be in violation of the Sherman and Clayton Acts. *United States* v. *American Can Co.*, 87 F. Supp. 18 (N. D. Cal.). In the subsequent proceedings to determine the appropriate remedy, the Government urged divestiture. In opposing such divestiture, American Can offered to undertake a closing equipment sales program as part of its business operations. The court approved this proposal. Accordingly, divestiture was not ordered. See *American Can Company* v. *C. I. R.*, 317 F. 2d 604 (2d Cir. 1963), *cert. denied*, 375 U. S. 993 (1964).

After negotiations between Continental and the Government with respect to the wording of the final judgment and decree to be entered against Continental, the court, on June 26, 1950, entered such a judgment and decree. In accordance with the provisions of the stipulation, divestiture was not ordered. Continental was directed, however, to cease its discriminatory closing equipment sales and leasing practices. The effective date of the injunctive provisions and the provisions concerning nondiscriminatory sales and leasing was January 1, 1951.

The decree stated, under the heading "Policy," that it was its purpose "to assure to those interested in owning container closing machines * * * the opportunity to purchase such machines * * * owned or controlled by defendant as of January 1, 1951," and that, with respect to equipment manufactured after such date, Continental was "to adopt a policy of affording to all those desiring such machines or equipment every available economic incentive to purchase such machines and equipment." Under the heading "Closing Machines—Sale," Continental was directed to sell, for a ten-year period, "to any applicant * * * in accordance with and subject to the provisions of this Judgment, any container closing machine which it owns on the effective date of this provision, or thereafter manufactures or ac-

quires." The decree further provided that existing lessees should, by a special communication, be advised of their prior right to purchase, at prices calculated in accordance with a formula established in the decree, the closing machinery then in their possession. Further, plaintiff was ordered in the future to sell or lease to any applicant machinery that it was then selling or leasing to its container customers. In order to insure that plaintiff complied with these and other provisions of the decree a special master was appointed to supervise such compliance, gather information regarding plaintiff's actions, and report to the Attorney General. (The master was the same one appointed pursuant to the corresponding portion of the American Can decree.)

Thereafter, plaintiff developed a program, including advertising materials, circulars, and specially prepared letters, to promote the sales of the equipment. Among other things, it furnished all of its lessees information concerning the methods, terms, and advantages of owning the equipment.

After January 1, 1951, plaintiff, in compliance with the decree, granted each of its closing equipment lessees an option to purchase and, further, embarked upon a general sales program designed to sell the machines.

Substantially all of the lessees then in possession thereafter proceeded to purchase the equipment. During the year 1951, plaintiff realized gross receipts of $4,005,899 from such sales of closing equipment which plaintiff had owned for more than six months prior to January 1, 1951. Net gains in the amount of $1,720,639 were realized from such sales.

In its 1951 tax return, plaintiff reported such sum of $1,720,639 as gains from the sale of capital assets held for more than six months. Section 117(j) of the 1939 Internal Revenue Code provides capital gains treatment for sales of

"property used in the taxpayer's trade or business," which is defined, insofar as is here pertinent, as property (a) of a character that is subject to a depreciation allowance, (b) is held for more than six months, and (c) is not "property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business."

However, when, in 1951 and the years thereafter, plaintiff sold closing equipment manufactured or acquired prior to 1951 to those not lessees-in-possession, or sold equipment manufactured or acquired after January 1, 1951, either to lessees-in-possession at the time of the sale or to those who were not leasing the purchased equipment at such time, it reported the gains derived from such sales as ordinary income.

After an audit of plaintiff's said 1951 tax return (by the District Director of Internal Revenue, Manhattan, New York), defendant made a determination that the $1,720,639 gain did not qualify for capital gains treatment because, in its opinion, the closing equipment constituted "property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business" under section 117(j). Accordingly, plaintiff's tax was recomputed on the basis of such gain's constituting ordinary income. On this basis, such amount also became includable in plaintiff's excess profits net income and was so included in defendant's recomputation of plaintiff's excess profits tax for such year.

After payment of the claimed deficiencies, with interest, plaintiff filed a claim for refund of income taxes (plus interest) in the amount of $3,157,721, or, in the alternative, for refund, even if the gain were held to constitute ordinary income under section 117(j), of the assessed deficiency with respect to the excess profits taxes (plus interest), in the amount of $1,327,518, such alternative claim being based on a contention that income of the type herein involved falls within the "abnormal income" exception contained in the

statutory provisions relating to the excess profits tax. More than six months having passed without any action on the claim having been taken by the Commissioner of Internal Revenue, the petition herein was timely filed.[2]

The Income Tax Issue

There is no dispute concerning the closing equipment in question constituting property subject to depreciation and, as of the dates of sale in 1951, having been held by plaintiff for more than six months. The only dispute between the parties is whether the equipment constituted "property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business." And, as stated, the only equipment involved in such dispute is that manufactured or acquired by plaintiff prior to January 1, 1951 (the effective date of the decree), which was on lease and sold to lessees-in-possession during the year 1951.

Plaintiff, pointing to the long period of time prior to 1951 during which it held the machines only for rental purposes, contends that, as of the 1951 sales dates, the machines had not been held "primarily" for sale to customers. The evidence shows that some machines sold in 1951 had been held by plaintiff as long as thirty years. The average age of the machines sold was at least 16.6 years.[3] Because of such extended period during which rental was the sole basis of holding, and, on a comparative basis, the brief period, *i.e.*, only portions of the year 1951, during which the machines had been held for sale, it becomes manifest, says plaintiff, that on an overall basis the property had been

[2] On June 30, 1964, which was after the filing of the petition on April 16, 1964, the Commissioner of Internal Revenue mailed to plaintiff a notice of disallowance in full of its claim for refund.

[3] The data upon which such computation was based takes the earliest acquisition date of any machine as 1920, although a substantial number of machines were in fact acquired before 1920. The average age is therefore actually greater than 16.6 years.

held "primarily" for rental and not for sale. And, it also argues, because of such long holding the gain resulted from a "'realization of appreciation in value accrued over a substantial period of time,'" *Malat v. Riddell*, 383 U. S. 569, 572 (1966), *i.e.*, the type of gain normally entitled to capital gains treatment.

Further, it contends that the closing equipment sales did not result from an activity arising from the "mainstream" and ordinary course of its business. Its business, says plaintiff, was the making and selling of whole, finished cans. The sealing to effect completion must be accomplished at the canner's plant after the cans are packed (the closing process, considered as sealing the tops on the cans, being identical with the process of fixing the bottoms to the cans, a process accomplished at plaintiff's own plants with substantially identical machines). Thus, plaintiff argues, the machinery only constituted part of its manufacturing facilities which produced the product it sold—cans. As such, the gains from the sales of the closing equipment, termed "productive capital goods," (Pltf. Brief, p. 5) were, it contends, "separate from the mainstream of the enterprise," and therefore entitled to receive the "more lenient treatment" afforded to capital gains as distinguished from the ordinary income treatment accorded "profits and losses arising from the everyday operation of a business * * *." *Recordak Corporation* v. *United States*, 163 Ct. Cl. 294, 298, 325 F. 2d 460, 462 (1963). The antitrust decree which, in effect, required the disposition of these capital assets, could not, it argues, serve to change the basic nature of the transaction, *i.e.*, a disposition of machinery that had been used for many years only to manufacture cans and that had never theretofore been offered as an independent sales item.

The very nature of the machinery sales compelled by the decree demonstrates, plaintiff further argues, that the sales were not made in the "ordinary" course of business.

Instead they constituted, it contends, unusual and extraordinary transactions. This is so, it says, because (a) the decree fixed the sales price of the machines located at the lessees' plants, thus depriving Continental of control over the price at which its own property was to be liquidated; (b) such prices bore no relation to fair market value (and in fact generally were below such value, as well as below replacement cost) and therefore "had nothing to do with the ordinary course of commerce"[4] (Pltf. Brief, p. 11); (c) plaintiff was deprived of customer choice (lessees-in-possession were, as shown, given priorities for the purchase of the equipment they were leasing); (d) plaintiff was deprived of the right to determine what machinery it would sell (again on the basis that the lessee had the right to purchase the particular machine he was leasing); (e) plaintiff could not even fix the payment terms (since the decree required it to grant installment credit terms to purchasers); and (f) the interposition of the special master's supervisory actions constituted an interference with plaintiff's conduct of its own operations.

For the following reasons, these contentions of the plaintiff cannot be accepted:

Where there is a change in the purpose of the holding of an asset, as there was here (as of January 1, 1951), the period of time prior to the date when such change took place, upon which plaintiff places such stress, is, even though lengthy as compared with the period of holding after such change-in-purpose date, not of importance in determining the "primarily" issue. The basic question is the primary purpose of holding as of the date of the sale. *Recordak Corporation* v. *United States, supra; Nadalin* v. *United States*, 176 Ct. Cl. 1032, 364 F. 2d 431 (1966).

[4] Since the machines involved had been held for such long periods of time, many had been fully depreciated. Consequently, even sales at the low decree price would produce gains.

And where a company is, at such date, regularly engaged in the dual business of selling and renting its machines, then income resulting from either activity satisfies the "primarily" concept, since it is "a part of" the "normal stream * * * of the taxpayer's business" and not "outside * * * [or] separate from the main-stream of the enterprise * * *." *Recordak Corporation, supra,* 163 Ct. Cl. at 298, 325 F. 2d at 462. In the similar *Recordak* case, the taxpayer, for over twenty years prior to 1950, only rented microfilming equipment. However, in that year "there was a change in operation," *i.e.,* the taxpayer, in order to obtain working capital, "decided that as of July 31, 1950, it would sell as well as rent all of its stock of microfilmers" (176 Ct. Cl. at 295, 325 F. 2d at 460), and this dual sale-or-rent business activity continued even after the taxpayer's need for working capital ended (in 1953). The continuance of the sales activity resulted from the introduction of a new model, the taxpayer thereafter deciding to dispose of the older equipment. This court rejected the taxpayer's claim to capital gains treatment for gains resulting from the sales of the older equipment. It held that such sales had, ever since 1950, formed "an accepted part of the taxpayer's regular business," and that "[i]f the purchasers are properly considered customers of that regular business, the taxpayer's dealings with them results in ordinary income." (163 Ct. Cl. at 298, 325 F. 2d at 462) And, specifically addressing itself to the "primarily" question in the case of a sale-or-rent operation, the court stated:

> Nor can plaintiff succeed in hitching its wagon to the word "primarily." Whatever the precise scope of that troublesome term in other contexts,[5] it does not exclude from ordinary income the proceeds of sales by one, like plaintiff, who conducts a dual enterprise involving both rentals and sales of the

[5] See Bernstein, *Primarily for Sale: A Semantic Snare,* 20 Stan. L. Rev. 1093 (1968).

> same type of goods. In that setting, "primarily" invokes a contrast, not between selling and renting, but between selling in the ordinary course of business and selling outside of that normal course. * * * [T]he goods are held "primarily for sale to customers in the ordinary course of * * * trade or business" because they are regularly offered for sale to customers as part of the normal operation of the enterprise. No case of this kind has allowed capital gains treatment. [163 Ct. Cl. at 300, 325 F. 2d at 463]

Thus, with the exception of the "liquidation" cases, *i.e.*, "where property has been sold [pursuant to an apparent businesslike activity] as a nonrecurring final disposition of a holding or business" (*id.*), when the sales income regularly results from the day-to-day conduct of a continuing business operation, as is here the situation, it makes no difference that a substantial part of the gain from such sales may have resulted from an increase in value which accrued during the longtime holding period prior to the change in purpose which resulted in the establishment of the business. *Recordak Corporation, supra; Nadalin, supra.* Accordingly, if one decides to go into business using as inventory property held for a long period which has increased in value and which, in accordance with the original purpose of acquisition and the immediately following holding, would, upon disposition, have been entitled to capital gains treatment, the conversion of such holding purpose and the resulting dedication of the property to a business-inventory purpose also serve to convert the proceeds from the sales of the property from capital gains to ordinary income.

The attempt to cast these sales in the "liquidation" mold of cases must also be rejected. Of course, in a certain sense, any sale, even of an ordinary item of inventory made in what everybody would agree was in the regular course of business, could be said to constitute the "liquidation" of an

"investment," for a businessman certainly "invests" in his inventory. However, the essence of the true liquidation cases in this tax law area is, as above stated, "the final disposition of a holding or business," such as small sales resulting from the inability to dispose of inherited or investment property en bloc, or the winding up (due to a reorganization, insolvency, etc.) of a business operation or a phase thereof.[6] The situation here, however, is the direct antithesis. The sales herein involved were made as an incident to the commencement of a new business, to be conducted on a permanent basis, and not as an incident to the winding up of an old one. The sales of identical machines manufactured or acquired subsequent to January 1, 1951, are conceded to constitute ordinary income, as indeed are sales of pre-1951 machines made to anyone other than a lessee-in-possession as of January 1, 1951. Only these particular sales are carved out as allegedly being entitled to special treatment. It seems obvious, however, that all sales of the equipment made after January 1, 1951, to customers for use in their canning operations should be treated alike and as part of the new business activity entered into as of such date.

Similarly, it is not possible to accept the contention that the sales were not made in the "ordinary" course of business because of the various regulatory terms of the decree. It is true that this phase of plaintiff's business, conducted as it was pursuant to the terms of an antitrust decree, was, naturally, regulated and supervised. But from the beginning plaintiff fought divestiture and sought to remain in the closing-equipment business. Its stipulation to abide by the results of the American Can litigation specifically excepted divestiture. It certainly knew that, if its activities were

[6] Cases illustrating these situations and allowing capital gains treatment are cited in *Recordak Corporation* v. *United States*, 163 Ct. Cl. 294, 299, 325 F. 2d 460, 463 (1963), and *Nadalin* v. *United States*, 176 Ct. Cl. 1032, 1043, 364 F. 2d 431, 437 (1966).

held to constitute transgressions of the Sherman and Clayton Acts, the conduct of this phase of its business operations, assuming it were permitted to remain therein at all, would necessarily, at least for a period of time, be required to be conducted pursuant to the terms of a decree. And when, after such illegality was established, American Can offered to make its machines available for sale as well as for rent, and, in connection therewith, to engage in a vigorous sales program, and thereby persuaded the district court not to order the divestiture for which the Antitrust Division was pressing, plaintiff accepted the same terms. It collaborated with the Government attorneys in fashioning the decree under which it would operate, including superintendence by the same special master who would supervise American Can's activities. For plaintiff, therefore, this newly established equipment sales portion of its overall business operations, conducted in accordance with the decree terms, would necessarily become its "ordinary" business. Plaintiff knew that the sale of the equipment to lessees-in-possession as of January 1, 1951, was one of the principal purposes of the new business upon which it was embarking. Many businesses are, for various reasons, subject to forms of regulation. This does not, however, make their everyday conduct in accordance therewith anything other than "ordinary," even though, despite their owners' deliberate choice to engage in such a regulated business, they might well prefer to conduct their business activities free of regulatory restriction.

Indeed, when this same contention was presented to the Second Circuit by American Can in its case involving the identical income tax issue as is here involved, the court considered the entire question of the reason why the taxpayer conducted this portion of the business as it did to be immaterial:

> But the taxpayer would have us read I. R. C. 1939, § 117(j)(1)(B) to require an ascertainment of its

subjective intent. It argues that, since it was the compulsion of the antitrust decree, and not business policy, that resulted in the closing equipment being held for sale, capital gains treatment is warranted. We feel the Commissioner is on sounder ground in contending for an objective approach. Irrespective of motive or cause, the fact remains that in 1953 the taxpayer held the machines for sale as part of its ordinary trade or business. * * *

* * * The fact of its subjective preference for its former—now illegal—manner of operation is singularly immaterial here. * * * [*American Can Company v. C. I. R., supra,* at 605-606]

The court went on to hold that plaintiff's position was not sustainable in any event because of its insistence on conducting this phase of its business under the terms of the decree:

We would note further that had the taxpayer been willing to divest itself of this line of its business, as was urged by the Antitrust Division, it would then have been entitled to capital gains treatment without question. Instead, the taxpayer chose, as the better of undesirable alternatives, to enter a new business: the sale, as well as the rental, of closing equipment. Thus, even looking to the motive or cause of the machines being held for sale, we cannot hold for the taxpayer. * * * [*Id.* at 606]

As indicated, it is only sales of pre-1951 machines to lessees-in-possession as of January 1, 1951, that plaintiff selects for special treatment. Plaintiff concedes that all other sales it made under its new sales program constitute ordinary income, and this would include even sales of pre-1951 machines provided they were not made to lessees-in-possession. It is plain, however, that these lessee-in-posses-

sion sales constituted only one segment of its newly adopted overall sales program. Pursuant thereto, and in accordance with the decree, plaintiff engaged in a comprehensive advertising program intended to inform its container customers who were then renting its machines that the machines were now available for sale at advantageous prices and terms. Plaintiff's regular container sales organization was given the added responsibility of vigorously attempting to sell the machines to lessees and other prospective purchasers. Through these efforts over the five-year period 1951-1955 plaintiff was able to sell approximately thirteen million dollars in machinery to lessees-in-possession as of January 1, 1951 (upon which approximately five million dollars in net gains was realized).

That the decree-regulated prices of the pre-1951 machines at which lessees-in-possession were privileged to purchase were much lower than the prices of the identical machines manufactured after January 1, 1951, is again only another of the conditions upon which plaintiff, knowing that it had been in violation of the antitrust laws and that the decree was intended to compensate for the illegal activity that had been engaged in, chose to enter this new business.[7] It is not surprising that, in prescribing formulae for maximum sale prices of the pre-1951 machines, the court obviously took into consideration the fact that the plaintiff's customers had been paying for the machinery during the previous years through their "tie-in" purchase of cans. For this reason and in the setting herein involved, the fair

[7] Plaintiff refers to the prices of the machines in question being "fixed" by the antitrust judgment or decree. However, the decree contained no set prices so "fixed." The judgment provided a formula for a maximum "base" price, *i.e.*, ten times 1950 rental, only provided, however, that the price resulting from such formula exceeded the "weighted average depreciated cost." If not, then such cost became the maximum price, provided it did not exceed the "current factory cost."

market value, replacement and manufacturing costs, and the fact that, as an abstract proposition, the maximum formulae selling prices of the machines were less than such value and costs, are irrelevant. Furthermore, it is also obvious that the court concluded that those who had been paying for the machines over the years should be given priority to purchase them.[8]"

Plaintiff distinguishes *American Can* on the grounds that that litigation covered not only pre-decree but also post-decree machinery, the treatment of which as ordinary income plaintiff does not contest, although American Can did. This distinction is hardly meaningful. Insofar as the decision did cover pre-decree machines, it is, clearly, directly in point. The pre-decree machines were not an insignificant nor unnoticed segment of the litigation, the court specifically observing that "[m]ost of the machines sold during the taxable year [there in question] were manufactured before the antitrust decree * * *." (*Id.* at 605)

Further minimizing *American Can* as authority, plaintiff points out that the court there, after reviewing the "impressive" number of machine sales the company made, and the intensity of its sales efforts, concluded that "[b]eyond question, American Can Company had a substantial purpose to sell its closing equipment." (*Id.* at 605) Plaintiff correctly points out, however, that in using such "substantial purpose" language, the court relied on a construction of the statutory clause "held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business" as meaning that a purpose may be "primary" if it is only "substantial," a doctrine which the Supreme Court rejected in *Malat v. Riddell, supra*. How-

[8] Although the decree required plaintiff to sell the machinery on credit if the lessee so desired, it also allowed plaintiff to require proof of satisfactory credit. There would appear to be nothing extraordinary about these provisions.

ever, although the Supreme Court in *Malat* specifically cited (n. 3, p. 571 *American Can* as one of the cases which had so erroneously interpreted "primarily," it in no way intimated that *American Can* had been wrongly decided, *i.e.*, that any different result would follow from the application of the proper test. *Malat* itself was an altogether different kind of case. It did not involve a taxpayer in two separate businesses, such as is plaintiff. There the taxpayer purchased and subsequently sold a parcel of land upon which it claimed capital gains treatment. The denial of such treatment resulted from a dispute between the taxpayer and the Internal Revenue Service as to the intended use of the parcel, the taxpayer claiming a purpose to hold and develop for a rental apartment project, and the Internal Revenue Service contending that the taxpayer had purchased and held the property either for such rental purpose or for the purpose of selling it, whichever turned out to be more profitable, and that since such possible sale constituted a "substantial" purpose of the holding, ordinary income treatment was justified. The district court had agreed with the Internal Revenue Service, and the Ninth Circuit affirmed. The Supreme Court, however, held that "'primarily' means 'of first importance' or 'principally'" and, without intimating "whether the result would be supportable on the facts of this case had the correct [legal standard] been applied," remanded the case to the district court for such application. (*Id.* at 572)

As shown above, this court, in *Recordak Corporation*, in a setting of a two business selling-or-renting case, concluded that "primarily" only "invokes a contrast, not between selling and renting, but between selling in the ordinary course of business and selling outside of that normal course," and that, in such a case, "the goods are held 'primarily for sale to customers in the ordinary course of * * * trade or business' because they are regularly offered for sale to customers as part of the normal opera-

tion of the enterprise." (163 Ct. Cl. at 300, 325 F. 2d at 463) Certainly here plaintiff, on a continuous day-to-day basis, and over the years, "regularly offered for sale to customers" the machines in question. Indeed, in *Recordak Corporation*, the court felt that the result in the "very close" (*id.*) two business sale-or-rent case of *American Can* conformed with the "primarily" test it was applying in *Recordak* and was proper. The Supreme Court, in noting, as aforesaid, the various interpretations that had been given to "primarily," including that in *American Can*, also noted (in the form of a "*Cf.*" following its citation of *American Can*) the *Recordak Corporation* decision without in any way intimating that the *Recordak Corporation* test was, in such type of two-business case, erroneous. Nor does plaintiff criticize *Recordak Corporation* in any manner. Instead, it merely contends that under the facts, the sales of the pre-1951 machines to the lessees-in-possession do not fall within the *Recordak* "mainstream" test. However, for the reasons set forth, the conclusion is compelled that they do.

And, just as the ordinary income result in the two business rent-or-sell *Recordak Corporation* situation is consistent with the "primarily" doctrine of *Malat*, so, as this court specifically held in *Nadalin* v. *United States*, *supra*, is there nothing inconsistent with *Malat* in the doctrine that ordinary income results from a change in the purpose of holding pursuant to which the property becomes devoted to a business purpose despite a long prior holding of a type that would have given rise to capital gains had such holding purpose persisted.

Finally, there surely is no merit to the contention that the sales in question were outside the "mainstream" of plaintiff's business because such business should be considered as one of selling completed, sealed cans, the closing equipment thus in effect constituting but a part of the total manufacturing process and therefore to be properly classified as productive capital assets. Plaintiff never conducted

its business operations in that manner. It always conducted the sealing operation as a separate business by charging rent for the closing equipment. Thus additional income traditionally resulted from this phase of its operations (although it is true that prior to the decree, plaintiff looked to the sale of its containers for a complete recovery of cost and a realization of its profit on both the sale of the containers as well as the rental of the equipment).[9] A manufacturer selling a completed product normally does not make a separate charge for an integral step in the productive process. Instead, all manufacturing costs are normally covered in the price of the completed product. All that happened here is that plaintiff's separate leasing business was expanded to a sale-or-rent business. Income from the sale of the machines was thus certainly in the "mainstream" of the closing equipment business that plaintiff had always conducted. Unless this portion of its operations had the status of a separate business, and not merely a step in the alleged basic manufacturing process of producing completed cans, there would have been no point in everyone, including plaintiff, treating it as a separate activity subject to and capable of divestiture.

In view of all of the above considerations, plaintiff is not entitled to recover on this aspect of the case.

THE ALTERNATIVE EXCESS PROFITS TAX ISSUE.

The determination by the Internal Revenue Service that the gains resulting from the sales of the closing equipment constituted ordinary income also had the effect of subjecting such gains to excess profits taxes under the Excess Profits Tax Act of 1950 (§§ 430-474, Internal Revenue Code of 1939). That Act was not applicable to gains from sales or exchanges of capital assets. (§ 433(a)(1)(c))

[9] Under the decree, which abolished the "tie-in" between the purchase of the cans and the leasing of the machines, plaintiff was required to cease charging only nominal rental amounts for the use of its machines and to establish realistic rental prices.

Plaintiff contends, however, that even if the gains herein involved are properly to be treated as ordinary income and therefore subject to the excess profits tax, they nevertheless constitute "abnormal income" within the meaning of section 456 of the 1939 Code, thus entitling plaintiff to the relief afforded by such section. Under this section the excess profits tax for a year in which such abnormal income is realized is computed by allocating a portion of such income to other years, *i.e.*, the previous or future years to which the income is attributable.[10] If such portions are allocable

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[10] Section 456 reads in pertinent part as follows:

SEC. 456. ABNORMALITIES IN INCOME IN TAXABLE PERIOD.

(a) DEFINITIONS.—For the purposes of this section—

(1) ABNORMAL INCOME.—The term "abnormal income" means income of any class described in paragraph (2) includible in the gross income of the taxpayer for any taxable year under this subchapter if it is abnormal for the taxpayer to derive income of such class, or, if the taxpayer normally derives income of such class but the amount of such income of of such class includible in the gross income of the taxable year is in excess of 115 per centum of the average amount of the gross income of the same class for the four previous taxable years, or, if the taxpayer was not in existence for four previous taxable years, the taxable years during which the taxpayer was in existence.

(2) SEPARATE CLASSES OF INCOME.—Each of the following subsparagraphs shall be held to describe a separate class of income:

(A) Income arising out of a claim, award, judgment, or decree, or interest on any of the foregoing; or

(B) Income resulting from exploration, discovery, or prospecting, or any combination of the foregoing, extending over a period of more than 12 months; or

(C) Income from the sale of patents, formulae, or processes, or any combination of the foregoing, developed over a period of more than 12 months; or

to years not subject to excess profits tax, the relief will, of course, be substantial. And even if the other years were

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(D) Income includible in gross income for the taxable year rather than for a different taxable year by reason of a change in the taxpayer's method of accounting.

* * *

(3) NET ABNORMAL INCOME.—The term "net abnormal income" means the amount of the abnormal income less, under regulations prescribed by the Secretary, (A) 115 per centum of the average amount of the gross income of the same class determined under paragraph (1), and (B) an amount which bears the same ratio to the amount of any costs or deductions relating to such abnormal income, allowable in determining the normal-tax net income for the taxable year, as the excess of the amount of such abnormal income over 115 per centum of such average amount bears to the amount of such abnormal income.

(b) AMOUNT ATTRIBUTABLE TO OTHER YEARS.—The amount of the net abnormal income that is attributable to any previous or future taxable year or years shall be determined under regulations prescribed by the Secretary. In the case of amounts otherwise attributable to future taxable years, if the taxpayer either transfers substantially all its properties or distributes any property in complete liquidation, then there shall be attributable to the first taxable year in which such transfer or distribution occurs (or if such year is previous to the taxable year in which the abnormal income is includible in gross income, to such latter taxable year) all amounts so attributable to future taxable years not included in the gross income for a previous taxable year.

(c) COMPUTATION OF TAX FOR CURRENT TAXABLE YEAR.—The tax under this subchapter for the taxable year, in which the whole of such abnormal income would without regard to this section be includible, shall not exceed the sum of:

(1) The tax under this subchapter for such taxable year computed without the inclusion in gross income of the portion of the net abnormal income which is attributable to any other taxable year. * * *.

This section was in effect only with respect to taxable years ending after June 30, 1950, and beginning before January 1, 1951. Section 430(a), Internal Revenue Code of 1939, as amended.

excess profits tax years, benefits will accrue because excess profits credits will become applicable for more than one year.

Included in the statutory classifications of income defined as "abnormal income" is "Income arising out of a claim, award, judgment, or decree, or interest on any of the foregoing;" (§ 456(a)(2)(A)). Plaintiff contends that the gains from the sales of the closing equipment fall within this classification since they "resulted from the fact of the antitrust decree.". That decree, says plaintiff, by "terminating Continental's policy of leasing closing equipment" and "forcing" the sales which resulted in the gains, was their producing cause. These gains therefore constitute, it contends, "income arising out of a * * * decree" within the meaning of section 456(a)(2)(A).[11]

Further, there is agreement that under section 456(b)[12] and the pertinent regulations,[13] the abnormal income must

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[11] Pltf. Brief, p. 18.

[12] See n. 10.

[13] Treasury Regulations 130 (1939 Code) provides:

"Sec. 40.456-3 Amount attributable to other years. (a) The mere fact that an item includible in gross income is of a class abnormal either in kind or in amount does not result in the exclusion of any part of such item from excess profits net income. It is necessary that the item be found attributable under these regulations in whole or in part to other taxable years. Only that portion of the item which is found to be attributable to other years may be excluded from the gross income of the taxpayer for the year for which the excess profits tax is being computed.

"(b) Items of net abnormal income are to be attributed to other years in the light of the events in which such items had their origin, and only in such amounts as are reasonable in the light of such events. To the extent that any items of net abnormal income in the taxable year are the result of such factors as high prices, low operating costs, increased demand, or decreased competition, such items shall not be attributed to other taxable years. Thus, no portion of an item is to be attributed to other years if such item is of a class of income which is in excess of 115 percent of the average income of the same class for the four previous taxable years solely because of an improvement in business conditions. In attributing items of

meet the additional requirement that it be attributable to other years. Plaintiff says the gain herein involved meets this requirement too because "such gain represents rental income Continental would have realized over a period of years had it not been for the effect of the antitrust decree." This conclusion is supported, plaintiff argues, by the fact that one of the formulae adopted by the decree to arrive at the "maximum base" price of the closing equipment herein involved is ten times 1950 rental. Thus, says plaintiff, the effect of the decree was to take rental income that would have accrued to plaintiff over ten years and condense it all into the one year of the sale. Such income is accordingly claimed as properly attributable to the ten-year period 1951-1961 and, therefore, allocable to such years. Plaintiff emphasizes[14] the language of Regulations 130, section 40.456-3(b) providing that "Items of net abnormal income are to be attributed to other years in the light of the events in which such items had their origin * * *"[15] (the "origin" of the "events" herein involved being, presumably, the antitrust decree).

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net abnormal income to other years, particular attention must be paid to changes in those years in the factors which determined the amount of such income. No portion of an item of net abnormal income is to be attributed to any previous year solely by reason of an investment by the taxpayer in assets, tangible or intangible, employed in or contributing to the production of such income."

[14] Pltf. Brief, p. 21.

[15] See n. 13. As set forth in n. 10, § 456(a)(1) provides that it must either be abnormal for the taxpayer to derive income of the particular class, or if the taxpayer normally derives income of such class, the amount of such income for the taxable year must be in excess of 115 percent of the average amount of the gross income of the same class for the four previous taxable years. In its normal course of business Continental has received income arising out of claims, awards, judgments, or decrees. Assuming the gain herein involved properly falls within such class, there is no dispute between the parties that the amount thereof received in 1951 is sufficiently in excess of income of the same class received by Continental in the four previous years to meet this 115 percent requirement.

These alternative contentions are not acceptable. In a sense, the gain plaintiff realized could, of course, be said to result "*from the fact* of the antitrust decree." [Emphasis supplied] In this sense, however, it could be said to have been realized from many "facts," *i.e.*, the "fact" of its corporate existence, or the "fact" that it was in the container business in the first place, or the "fact" that it had indulged in illegal activities prior to the decree. Clearly, however, this is not the sense in which the statute exempts "income arising out of a claim, award, judgment, or decree." It seems plain that what is here referred to is moneys flowing from some kind of affirmative assertion of claim by the taxpayer, a claim that may have been successfully prosecuted and thus have taken the form of an "award," a "judgment," or a "decree," all of which are common terms used to describe the final actions of judicial or quasi-judicial bodies in determining, after adjudicating a dispute, that a claimant is entitled to a certain sum of money. "Judgment" is, of course, the common term applicable to the final action of courts in proceedings to enforce rights and to determine amounts due. In certain actions, especially those of an equitable nature, or those determined by admiralty or probate courts, the final determination, including the requirement that a certain amount be paid by one party to another, may take the form of a "decree." See *National Surety Co.* v. *Halligan*, 105 N. J. L. 336, 146 A. 372 (1929) (involving a judgment type of decree of a surrogate's court requiring the payment of a certain sum by one party to another). An example of a decree under which monetary damages may be awarded is that which may be rendered in a patent infringement suit. "A patent owner ordinarily has his election to sue at law charging infringement and demanding damages, or he may seek an injunction, accounting and damages in equity." *Ryan Distributing Corporation* v. *Caley*, 51 F. Supp. 377, 379 (E. D. Pa. 1943), *aff'd* 147 F. 2d 138 (3d Cir.

1945), *cert. denied,* 325 U. S. 859.[16] These determinations are also, of course, frequently denominated "awards," and such "award" language is also commonly used in connection with arbitration proceedings. Thus, all the "claim, award, judgment, or decree" language involves terms customarily associated with an affirmative assertion of moneys due (a "claim") and some formal determination thereof (an "award, judgment, or decree"). It seems plain that this was what the provisions herein involved, being addressed to "abnormal income" and income "attributable to other years," meant, for it might, for instance, take many years to establish a claim based upon past events or contracts, and it was obviously felt that it would not be fair to throw the recovery into income subject to the excess profits tax if the litigation happened to be concluded in a year in which such a tax was in effect. See *Bell Aircraft Corporation,* 32 T. C. 355 (1959) (Court of Claims judgment allowing a recovery with respect to expenditures made in the performance in prior years of cost-plus-fixed-fee contracts held to constitute "income arising out of a * * * judgment," and which income was "attributable to other years"). Accordingly, "judgment" or "decree," in the "claim, award, judgment, or decree" context could hardly encompass an antitrust "Final Judgment" such as is here involved, which had no purpose of adjudicating any monetary claim or demand that plaintiff was pressing but which instead "Ordered, Adjudged and Decreed" that plaintiff, as a defendant, cease its illegal practices and required it to make its closing equipment available for sale as well as for rent. The statutory classifications of "income" which are to be treated as "abnormal income"[17] in no way evidence an in-

[16] In Treas. Reg. 130, § 40.456-6(b), a recovery in a patent infringement suit is cited as a possible subject for relief under the abnormal income provisions.

[17] See n. 10.

tention to convert "ordinary income" to "abnormal income" simply because the change in holding purpose which led to the establishment of the new "trade or business" came about in order to be in compliance with an antitrust judgment or decree.

In *Yuba Gardens, Inc.*, 17 T. C. 334 (1951), moneys received by the taxpayer in the ordinary course of business were likewise refused "abnormal income" status since they were not received pursuant to a "claim" within the meaning of a similar excess profits tax act. There the taxpayer sold parcels of land under contracts which required payments to be made over the succeeding ten years. During the taxable year in question the taxpayer received, in addition to the regular installments, delinquent as well as accelerated payments. Because of the requirement that all of the unusually large amount of receipts be included in the taxpayer's gross income in the year of receipt, it sought to have the payments considered as abnormal income arising out of a "claim" pursuant to the provisions of the predecessor of section 456. The Tax Court, however, denied the requested relief under the excess profits tax law, stating:

> * * * Although it does not seem that Congress intended to restrict the meaning of the term "claim" to technical items such as litigated claims, it does appear that something more than an existing right is necessary to come within the intendment of the statute. *Since the term is used in connection with "award, judgment, or decree," it appears that at the least the statute requires that there be a bona fide dispute or an asserted demand.* [Emphasis supplied] (at 343)

Even as to the delinquent payments, the court noted that the taxpayer had never made any demands to enforce its

contract rights but simply permitted the purchasers to make payments as they could.

Neither of the two cases plaintiff cites, *Bell Aircraft Corporation, supra,* and *Triboro Coach Corporation,* 29 T. C. 1274 (1958), in both of which "abnormal income" status was accorded the amounts in dispute, supports its position that an antitrust "judgment" or "decree" such as is here involved would fall within the terms of the section. Both cases involved money recoveries as a result of affirmative claims asserted and pressed by the taxpayer, *Bell Aircraft* involving, as stated, moneys received under a Court of Claims judgment, and *Triboro Coach* involving moneys ultimately received as a result of a dispute between a bus operator-taxpayer and New York City over the amount of a service charge to be allowed the bus company for the performance in prior years of certain functions (printing, selling, collecting and accounting) in connection with "combination" rides on the taxpayer's and the city's lines. In *Triboro Coach,* the Tax Court held the amounts so received by the taxpayer to constitute income "arising out of a claim," stating:

> It is clear from the testimony that Triboro was pressing a request for an increased allowance for the performance of the functions for which the service charge was provided. * * * There was *at least a dispute or an asserted demand* sufficient to constitute a "claim." [Emphasis supplied] (at 1280)

Similar "abnormal income" was recovered by the taxpayer who pressed "asserted demands" in *American Enka Corporation,* 30 T. C. 684 (1958) (recovery of interest on tax over-assessments).

All of these cases illustrate what clearly appears to be the common understanding of "income arising out of a claim, award, judgment, or decree," and support the con-

clusion that plaintiff's income arising out of sales of pre-1951 container-closing equipment to lessees-in-possession, made in compliance with the antitrust decree, does not qualify for relief under section 456.[18]

Additionally, even if plaintiff's interpretation of the "decree" provision be considered proper, so that the gain herein involved could be treated as "abnormal income," it seems plain that the gain neverthless does not meet the "attributable to other years" requirement. The ground upon which plaintiff relies, *i.e.*, that the antitrust judgment provided that the maximum "base" price of the pre-1951 machinery located at the lessee-canners' plants should be ten times the 1950 rental, so that the gains therefore are properly attributable to the ten-year period 1951-1961, is not persuasive. The conversion into a lawful sales price of what would, under the old, illegal, system, have been rental income for ten future years could hardly be considered as producing, as a result of sale, income "attributable" to such years. In the first place, when an article may be either rented or purchased, it would not seem unusual to have the sales price and the rental fee bear some kind of a ratio relationship. However, this does not make, in any real sense, the income from the sale any the less "attributable" only to the year of the sale, for both the sales price and the rental fee obviously stand on their own feet. Such sales income could hardly be considered as attributable to the years which would hypothetically have produced

[18] The comparison of the 1951 gain here involved with the "income arising out of claims, awards, judgments; or decrees" which plaintiff realized during the years 1947 through 1950, which comparison is set forth in the record as proof of eligibility under the 115 percent provision of sec. 456(a)(3) (see n. 10), also shows that such 1947-1950 income was of such affirmative-claim-money type which plaintiff had asserted, *i.e.*, "State & Local Tax Refund and Interest," "Bad Debt Recoveries," and "Other claims (freight)." (Finding 51)

rental income had the sales not been effected. It seems quit clear that what was intended to be covered were situations permitting more definite and precise "other year" income attributions, such as, for instance, the *Bell Aircraft* situation, where moneys due under completed contracts were not received until protracted litigation finally produced them in a later, but excess profits, tax year. In all of the above-cited cases allowing "abnormal income" relief, the attribution of the income to other years was based on some such similar factor. Secondly, in this particular instance, it is all the more difficult to regard the sales price as "attributable" to the rental income which would have been produced over a ten-year period when it would have been illegal for plaintiff to have continued to rent the equipment during 1951-1960 on the old 1950 rental basis and method of doing business.[19]

For all of the reasons hereinabove set forth, it is concluded that plaintiff is not entitled to recover.

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[19] As shown in n. 7, the ten times 1950 rental maximum sales price formula was not the exclusive method under the decree for the establishment of the sales price. If such price was less than the "weighted average depreciated cost," such cost became the "base" price. This price, however, could not exceed the "current factory cost" of the type and model involved on the effective date of the decree. Furthermore, the equipment covered by the decree embraced not only the closing machine itself but certain "related equipment" and "auxiliary equipment" and in the case of such equipment, the decree simply required "reasonable, uniform and nondiscriminatory" sales prices if Continental had no established rental rate therefor in effect for the calendar year 1950. Thus, there is no showing that all of the sales receipts herein involved represent the "ten times 1950 rental" formula. Such "related equipment" is used in various ways incident to the closing operation, including the preparation, filling, or weighing of the contents of the can prior to final seaming. Similarly, the "auxiliary equipment" consists of such mechanisms as nonspill devices.

Dissenting Opinion

SKELTON, *Judge*, dissenting:

I respectfully dissent.

The only property involved is the can closing equipment which the plaintiff had been leasing to its customers for 16.6 years on the average and in some cases for thirty years.

The only problem involved is whether this equipment constituted "property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business."

In my opinion, this property was not only *not* held "primarily" for sale to its customers, but was not held for sale at all. Furthermore, when taxpayer was forced to convey the equipment to its lessees by the court decree, this was not done in the ordinary course of business but in a most extraordinary way.

The courts have uniformly held where this problem has arisen that it must be solved by the facts in each particular case and that there is no formula or rule of thumb test that can be applied to all cases. For this reason, this case must be considered in the light of its peculiar facts that are not to be found in any other case.

We start with the Supreme Court's definition of the word "primarily" in the case of *Malat v. Commissioner*, 383 U. S. 569 (1966), where the courts said:

> * * * We hold that, as used in § 1221 (1) [Sec. 117 (j) of the Internal Revenue Code of 1939] "primarily" means "of first importance" or "principally." [*id.* at 572.]

This definition in effect overruled *American Can Co. v. Commissioner*, 317 F. 2d 604 (2d Cir. 1963), *cert. denied*, 375 U. S. 993 (1964), which the Supreme Court referred to in footnote 3, page 571, as being one of the cases where there

was a conflict over the meaning of the word "primarily." It will be noted that in *American Can* the court had said that "primarily" meant "substantial" instead of "principal." The majority relies heavily on *American Can* in this case, but obviously its reliance thereon is misplaced because the decision of the Supreme Court in the *Malat* case has effectively negatived its standing as an authority in this field. Moreover, *American Can* is clearly distinguishable on the facts from the instant case. There, the taxpayer evidently repossessed or reclaimed its leased machines from its lessees and put them in its inventory or stock of merchandise held for sale, although this is not made clear by the opinion. However, we can assume this is what happened because it is clear that after the decree of 1950, it sold all machines, both those previously leased as well as new ones manufactured after the decree, to the general public indiscriminately during the years 1951, 1952, and 1953. It then claimed it was entitled to capital gains treatment for *all* machines (both old and new) sold by it in 1953 only. As is evident, 1953 is a taxable year more than three years after the decree was entered, and during these three years it sold *all* machines to *all* people and then claimed the exemption on *all* sales. These facts are not present in our case. Consequently, *American Can* does not control our case either on the facts or on the law.

In the *Malat* case, the Supreme Court also mentioned *Recordak Corporation* v. *United States*, 163 Ct. Cl. 294, 325 F. 2d 460 (1963), which the majority relies on, with a *cf.* reference to it in the same footnote described above in which it listed *American Can*. In other words, it was listed among the cases where a conflict existed as to the meaning of the word "primarily." The majority says that the Supreme Court did not intimate that *Recordak Corporation* was erroneous. I disagree at least as to the meaning of the word "primarily," because otherwise there would have been no reason to list it with *American Can* and the other

cases that had erroneously defined "primarily" in the Code. This is made doubly apparent by a reading of the opinion in *Recordak Corporation* in which this court said in defining "primarily":

> * * * [G]oods are held "primarily for sale to customers in the ordinary course of * * * trade or business" because they are regularly offered for sale to customers as part of the normal operation of the enterprise. * * * [*Id.* at 300.]

In my opinion, this statement does not meet the requirements of the Supreme Court's definition. The word "regularly" has about the same meaning as "substantially" which was erroneously used in *American Can* to define "primarily." Goods could be "regularly" offered for sale without being "principally" offered for sale and without sale being the object of "first importance" in the offering. They could be offered "principally" for lease and with rentals being of "first importance," even though "regularly" offered for sale. In such case, under the Supreme Court's definition, the goods would not be held "primarily" for sale, and any gain by the taxpayer on their sale would be long term capital gain under Section 117(j) of the Code.

In any event, the *Recordak Corporation* case does not require a decision against the taxpayer in our case as a matter of law, nor even as a compelling precedent. We do not have to overrule that decision in order to hold for the taxpayer here. That case, in addition to the foregoing, is clearly distinguishable from the instant case on the facts. There, the taxpayer had been freely and voluntarily disposing of its microfilm machines either by rental or by sales to anyone wishing to acquire them for over four years prior to the tax years in question. The machines were in its possession and inventory as the main part, if not the only part, of its stock of merchandise. When a new model came out, it decided to

dispose of the old machines. This was accomplished by selling what it could and discarding the rest as junk. It claimed capital gains treatment for the equipment thus disposed of, which was correctly denied. It was never intended that capital gains treatment would be given to transactions of that kind. Otherwise, every time a new model automobile or appliance came out, the dealer could dispose of his old models and claim capital gains treatment for any profit made.

The facts in our case are vastly different. Here, the taxpayer had been leasing the machines for over thirty years (their average age was more than 16.6 years). It had never sold nor offered to sell any of these machines during this entire period. At the time of the decree in the antitrust suit, the machines were not even in its possession but were in the hands of the lessees who had the right to such possession under the terms of the leases. Consequently, they were not a part of its inventory nor stock of merchandise on hand and they could not have been offered for sale to the general public prior to the decree because of the lease contracts. It should be remembered that we are only considering the leased machines (and not machines in general) because they are the only ones involved here. Under these circumstances, everyone will agree that up to the time of the decree, the taxpayer did not hold these machines "primarily for sale to customers in the ordinary course of his trade or business." In fact, it made no sales and refused to make them. As far as these machines were concerned, it was in the leasing and rental business exclusively.

The defendant says in its brief (page 11) that "* * * whether goods are being held primarily for sale in the ordinary course of business depends * * * upon conditions *at the time of sale.*" [Emphasis supplied.] I do not agree. This argument would require us to shut our eyes to the purpose for which the machines were acquired and the purpose for which they were held and used during the 30 years

they were leased, and would require us to look only to the fact that they were sold as proof they were being held primarily for sale. The same argument could be made if the taxpayer was forced to make the sales at gun point, but no court would hold that sales under such circumstances would be proof that the goods were being held primarily for sale. The situation before us is not materially different, especially when the end result is considered. Here, the taxpayer was forced to sell these machines at "legal gun point" (the decree), when it did not want to do so. It had no choice as to whom the machines would be sold, nor the price to be obtained for them nor the terms of sale. The decree took care of all of these matters and forced the taxpayer to comply with its dictates. Yet, the government would have us consider only the fact that sales were made "at the time of sale," and asks us to hold that the sales made under these circumstances were made in the normal course of business as ordinary sales. They could not have been more extraordinary unless physical force had been used. There was nothing normal about them.

This "at the time of sale" argument was answered by the court in *Philber Equipment Corp.* v. *Commissioner*, 237 F. 2d 129 (3d Cir. 1956). There the taxpayer was in the business of renting motor vehicles (trucks, tractors and trailers) to the public. Most of the leases were for one year. When the vehicles were returned at the end of the leases, they were not worn out but still had a lot of useful life left in them. The taxpayer sold them and claimed long term capital gain. The Commissioner rejected the claim and said that only ordinary gain applied because the vehicles were acquired for the dual purpose of leasing and selling, and, therefore, they were held primarily for sale. This was upheld by the Tax Court. However, the Circuit Court of Appeals reversed this decision and held for the taxpayer. It said that:

> * * * [T]he determinative factor is the purpose for which the property was held at the time of its acqui-

> sition and during the period of its use. * * * [*Id.* at 131.]

The court also said that the sale, standing alone "cannot be considered inconsistent with the conduct of a rental business or make the sale factor a dominating business purpose of the taxpayer." [*Id.* at 132.] The court held that notwithstanding the sales, the "primary business purpose was vehicle rental." In that case, the same "at the time of sale" argument was made as in the instant case, which was upheld by the Tax Court but rejected by the Court of Appeals when it said:

> The Tax Court, as an alternative ground, stated that even if the intention to sell had been absent at the time of the original acquisition, such intention did exist at the time of re-possession from the lessee, and the determining factor is then the purpose for which the property was being held at the time of sale rather than the purpose for which it was originally acquired and held.
>
> We cannot subscribe to this "alternative ground". To do so would make for judicial nullification of Section 117(j).
>
> The essence of the Tax Court's alternative ground is that property changes character merely by the fact of its being exposed for sale. We agree with the taxpayer that such a concept is neither logical nor reasonable. [*Id.* at 132-33.]

In my opinion, the conditions that existed at the time of the decree are more important than those which existed at the time of the sale. For all practical purposes, the sales were required and arranged for at the time the decree was entered. At that time, the taxpayer was required to sell the leased machines to the lessees who had possession of them for the prices and on the terms specified in the de-

cree. All that remained to be done were the purely routine and perfunctory acts of transferring title. As far as the taxpayer was concerned, the sales were made by the decree at the time it was entered. No one—not even the Commissioner of Internal Revenue with his ever changing ability to be fluid in problems of this kind[1]—could contend that the machines were being held primarily for sale at the time the decree was entered.

The majority opinion stresses the point many times that the taxpayer entered into a *new* business on January 1, 1951, after the decree had been entered on June 26, 1950, which had a dual purpose of leasing and selling the same kind of machines that are involved in this case. This is true, but the *new* business had nothing to do with the *old* business of leasing the machines which were already committed to be disposed of under the decree before any new business was started. The machines leased under the old business which were sold to the lessees under the decree, were never repossessed, never put into stock, never became a part of taxpayer's merchandise inventory, and never offered to anyone for sale except to the lessees, who had possession of the machines, after the decree was entered. They never became a part of the new business, but were disposed of when the old business was closed out by the decree. There was a forced divestiture of the leased machines by the order of the court, and this divestiture became binding when the decree was entered.

There have been many cases where property has been acquired and held for the dominant purpose of rental or for some other dominant purpose, not including sale, and when the property was finally sold, the fact that a sale was made did not deprive the taxpayer of capital gains treat-

[1] See *Dunlap* v. *Oldham Lumber Co.*, 178 F. 2d 781 (5th Cir. 1950), where the Commissioner took a position different to that taken by him in the instant case.

ment under Section 117(j). For instance, in the case of *Delsing* v. *United States*, 186 F. 2d 59 (5th Cir. 1951), the taxpayer was in the business of building and selling homes. He built 45 rental houses under Federal Housing Administration regulations in which he agreed to construct them for rent. The tenants were given the right to buy the houses after a stated period of time on specified terms. Before building the houses, he wrote a letter to the FHA saying "these houses are to be built for sale or rent." The houses were rented for three years and were then sold to the tenants. The taxpayer claimed capital gains treatment, which was denied by the IRS, which contended that the houses were held primarily for sale as shown by the letter and because they were sold. The court held for the taxpayer, saying the houses were capital assets and were not held primarily for sale in the ordinary course of taxpayer's business. It would appear that the instant case is stronger for the taxpayer than the cited case.

In the case of *Dunlap* v. *Oldham Lumber Co.*, *supra.*, N. 1, the taxpayer was in the lumber business. It bought fifty vacant lots in a subdivision in 1928 with the unrealized expectation that they would be taken into the city limits and public utilities made available. It had hoped to sell lumber to build homes to individuals who would purchase the lots. It sold a few lots from time to time. During one five-year period it sold only one or two lots. Finally, it sold 27 of the lots in 1944 and the remainder in 1945 at a loss. It claimed an ordinary loss on its income tax returns, but this was denied by the Commissioner who held that the lots were capital assets and were not held primarily for sale and the loss was a capital loss and not an ordinary loss. (It will be noted that the Commissioner took exactly the opposite position there than he is taking in the instant case.) The court held:

> * * * The conclusion is inescapable that the sale of the lots was most *extraordinary and not at all ordi-*

> *nary*, and there was no ordinary course of business as to lot sales. By the express terms of the statute property must not only have been "held primarily for sale," but also for sale in the "ordinary course of the business of the taxpayer." * * *
>
> We conclude, therefore, that * * * the lots in question were capital assets, * * *. [Emphasis supplied.] [*Id.* at 785.]

It is significant that in that case the taxpayer intended to eventually sell the lots at the very time it purchased them and actually did sell them in the end. However, the Commissioner paid no attention to these facts and contended the taxpayer did not hold the lots primarily for sale. Yet, in the instant case the Commissioner says that because there were sales, the machines were held primarily for sale. Of course, in that case, the Commissioner was trying to prevent the taxpayer from taking an ordinary loss while here he is attempting to prevent the taxpayer from receiving capital gains. It is amazing how agile he can be in shifting positions when to do so is against the taxpayer and in favor of the government.

The case of *United States* v. *Bennett*, 186 F. 2d 407 (5th Cir. 1951) is in point.[2] There, the taxpayer was in the business of breeding cattle to sell the calves and these sales constituted the main source of his income. In addition, however, when cows or bulls were no longer useful for breeding purposes, he would cull them out of the herd and sell them. His business was a continuing one. He claimed capital gains on the sale of these culls, but the Commissioner contended that the taxpayer intended to eventually sell every calf born, either as a calf or later on as a cull, and, therefore, all of the cattle were held primarily for sale. The court ruled in favor of the taxpayer and upheld his

[2] See also *Davidson* v. *Tomlinson*, 165 F. Supp. 455 (S.D. Fla. 1958).

contention that the cattle were kept primarily as breeders and not for sale and that their sale when they were no longer useful as breeders was purely a secondary or incidental use. In so holding, the court said:

> If the statute had been intended to mean what the collector contends for, the word "primarily" would not have been in it. Since "primarily" is in the statute, it seems clear to us that to hold, as the collector contends, that the main, the first, purpose of the keeping of these breeder cattle was for sale, does complete violence to the statute and to its purpose and intent.
>
> The construction contended for by the taxpayers seems the more reasonable to us. It has the support of the *Albright* v. *United States*, 8 Cir., 173 F. 2d 339, and of two tax cases, *Emerson* v. *Commissioner*, 12 T.C. 875; *Fawn Lake Ranch Co.* v. *Commissioner*, 12 T.C. 1139; and in principle of *Delsing* v. *United States*, 5 Cir., 1951, 186 F. 2d 59. [*Id.* at 411.]

The principal factor that is determinative of whether property is held primarily for sale, according to the cases where the problem has arisen, seems to be the purpose for which it was acquired and held during the period of its use. The fact that it is finally sold is not the dominating nor controlling factor. This was aptly stated by the court in *Philber Equipment Corp.* v. *Commissioner*, 237 F. 2d 129 (3d Cir. 1956), as follows:

> The essence of the Tax Court's alternative ground is that *property changes character merely by the fact of its being exposed for sale.* We agree with the taxpayer that such a concept is neither logical nor reasonable. [Emphasis supplied.] [*Id.* at 133.]

In the instant case, the machines were acquired and held for 16.6 years on the average and some of them for 30 years

for the sole purpose of renting or leasing them. They were rental property and were not held primarily for sale in the ordinary course of the taxpayer's business. In fact, as stated above, they were not held for sale at all and no sales were made. The decree could not change the character of these machines overnight by requiring that they be sold to the lessees. Furthermore, the decree ordered them sold in a most extraordinary manner that was not in the normal course of business of the taxpayer.

For all of these reasons, and in accordance with the foregoing authorities, I would hold that as a matter of law plaintiff is entitled to recover and would enter judgment accordingly.

COLLINS, *Judge*, and NICHOLS, *Judge*, join in the foregoing dissenting opinion.

FINDINGS OF FACT

1. Plaintiff is a New York corporation having its principal office at 633 Third Avenue, New York, 17, New York. Plaintiff filed its income tax return for the taxable year ending December 13, 1951, with the District Director of Internal Revenue, Upper Manhattan, New York.

2. Plaintiff filed on or about March 17, 1952, its federal income and excess profits tax returns for the calendar year 1951, disclosing an income tax liability of $12,385,811.94 and an excess profits tax liability of $1,434,050.39 for a total liability of $13,819,862.33; which amount was paid to the aforesaid District Director as follows:

March 15, 1952	$ 4,837,462.33
June 16, 1952	4,837,000.00
September 15, 1952	2,072,700.00
December 15, 1952	2,072,700.00
Total	13,819,862.33

Findings of Fact

3. On or about December 31, 1952, plaintiff filed amended federal corporation income and excess profits tax returns for the calendar year 1951, disclosing additional income tax liability in the amount of $135,854.46 and excess profits tax liability of $69.33 for a total tax due of $135,923.79, which tax was paid in full by plaintiff on or about December 31, 1952, to the District Director of Internal Revenue, Upper Manhattan, New York.

4. On or about May 14, 1953, the District Director of Internal Revenue, Upper Manhattan, New York, refunded to plaintiff an overpayment of excess profits tax for the calendar year 1951 in the amount of $1,251,030.56, said refund resulting from the tentative carryback to that year of an unused excess profits tax credit for the calendar year 1952.

5. The phrase "closing equipment," as used in this case means "container-closing machines" and "related equipment," which terms have the same meaning herein as that set forth in Section I, paragraphs C and D, respectively, of the Final Judgment, dated June 26, 1950, entered by the United States District Court for the Northern District of California in the case of *United States of America* v. *Continental Can Co., Inc.*, Civil Action No. 26346 (hereinafter sometimes referred to as the "antitrust decree" or "decree").

6. Plaintiff, since its incorporation on January 17, 1913, has engaged in the business of manufacturing and selling various containers for food, beverages, and other products.

7. From 1913 to June 26, 1950, as a part of its business of manufacturing and selling containers, plaintiff manufactured or acquired and installed at the plants of its customers for containers the closing equipment required to affix covers to, or otherwise close, the containers sold by plaintiff, and for other operations connected with the closure of such containers.

Findings of Fact

8. The closing machines, which served the purpose of sealing the tops of customers' containers after being filled with the product, were substantially identical and interchangeable with machines used by plaintiff in its own operations involving the process of affixing the bottoms to containers which were sold to customers. The machinery plaintiff used in its own operations to affix the bottoms to containers could be and was withdrawn from such activity and leased to canners for use in closing their containers, *i.e.*, affixing the tops. Furthermore, such machinery was reacquired by plaintiff for use again as bottom affixers in plaintiff's operations and ultimately these machines were disposed of by sale or otherwise.

9. Prior to 1951 the closing machines leased by plaintiff could not be used to close cans made by a manufacturer other than plaintiff unless certain modifications and adjustments were made to the machines. This condition continued through the year 1951.

10. From 1913 to June 26, 1950, it was plaintiff's policy and established practice to lease rather than to sell its container-closing machines and to lease such equipment only to its container customers. No sales took place during this period except for a few isolated ones to the Government and to plaintiff's foreign subsidiaries. During said period, the lessees of closing equipment under lease with plaintiff were given no option to purchase such equipment.

11. Prior to 1951, the rentals generally charged by plaintiff for closing equipment were not intended to reimburse and did not reimburse it for the cost of furnishing and servicing such equipment and to provide a fair profit thereon, but plaintiff looked to the sale of metal containers for a complete recovery of cost and a realization of a fair profit on both metal containers and closing equipment. As a result, plaintiff often charged nominal rentals for such equipment.

Findings of Fact

12. On August 27, 1946, the United States of America commenced an action (Civil Action No. 26346-R) against plaintiff in the United States District Court for the Northern District of California, and on June 7, 1948, filed its amended complaint alleging violations of the Sherman and Clayton Acts. Plaintiff filed its answer and an amended answer to the aforesaid complaint and amended complaint denying the material allegations thereof.

13. At the same time, and upon substantially similar grounds relating in part to the common unlawful practice of tying the sale of containers into the leasing of container-closing equipment, the United States of America also commenced an action (Civil Action No. 26345-H) in the same federal district court against American Can Company. American Can Company and Continental Can Company were the two largest competitors in the container industry during the time of the antitrust proceedings.

14. The amended complaint in the antitrust suit of *United States of America* v. *Continental Can Company, Inc.*, filed on June 7, 1948, included in its prayer for relief the following:

> 5. Divesture of the closing machine part of defendant's business, that is, the manufacture, ownership and leasing of closing machines by defendant; or
>
> 6. Adjudging the total requirements contracts between defendant and its lessees and customers to be illegal and ordering defendant to cancel the same and to refrain from enforcing them; and directing defendant to sell or lease its closing machines to any applicant on non-discriminatory terms and conditions and to provide service for said machines to all lessees on the same terms and conditions.

15. Pursuant to a stipulation between plaintiff and the United States of America, dated September 30, 1949, and

filed with the United States District Court for the Northern District of California on October 7, 1949, the parties agreed that further proceedings in the Continental action should be suspended until after a final decision in the *American Can* case. Continental consented to the entry of a decree in its case in substantially the same terms as might be entered against American Can in its case. This agreement was qualified by plaintiff to the extent that any decree entered against it should contain no provision for divestiture of its closing machines, even though such provision for divestiture may be contained in the decree against American Can Company. In the event divestiture would be ordered against American Can, plaintiff reserved the right to litigate whether divestiture should similarly be adjudged as a part of the relief against it. The stipulation further provided that any decree against Continental should be entered at approximately the same time as the decree entered against American Can and be made effective simultaneously with such decree. A further provision was to the effect that if the complaint against American Can was dismissed on the merits, the complaint against Continental would be similarly dismissed, and that in the event of a dismissal without prejudice, Continental could then litigate all factual and legal issues involved in the action against it.

16. Plaintiff participated in discussions with Government counsel with respect to the wording of the final decisions and decrees. On June 26, 1950, after extensive hearings, the district court rendered its "Final Judgment" in the aforesaid antitrust action against plaintiff, in which it was "Ordered, Adjudged and Decreed," among other things, that plaintiff cease its tie-in arrangements and that plaintiff make its closing equipment available for sale or lease to any applicant. Section II of the judgment contained the various "Injunctive Provisions" and Section III, headed "Machines and Equipment," the provisions requiring the sale thereof and setting forth pricing formulae.

17. The antitrust decree ended plaintiff's practice of charging nominal rentals for the leasing of container-

closing equipment and directed plaintiff to adopt a more reasonable pricing program with an eye toward attaining compensatory rentals within three years which were to take into account the expenses incurred by plaintiff in the leasing of the machines, including depreciation, a reasonable return on the investment, and the cost of providing services in connection with the leasing. Renting the machines at the increased compensatory rental would have produced a greater income for plaintiff than selling the machines at the decree price.

18. The purpose of the decree in fixing the terms of the nondiscriminatory sales and leasing of container-closing equipment is set forth in Section III, as follows:

> *Policy*
>
> 1. It is the express purpose of this Judgment to assure to those interested in owning container closing machines, related equipment and auxiliary equipment, the opportunity to purchase such machines and equipment owned or controlled by defendant as of January 1, 1951; and, with respect to container closing machines, related equipment and auxiliary equipment manufactured or acquired by defendant after January 1, 1951, for defendant to adopt a policy of affording to all those desiring such machines or equipment every available economic incentive to purchase such machines and equipment.
>
> *Closing Machines—Sale*
>
> 2. Defendant is hereby ordered and directed to sell, for a period of ten (10) years from the effective date of this provision, to any applicant, for use, sale or lease in the United States, in accordance with and subject to the provisions of this Judgment, any container closing machine which it owns on the effective date of this provision, or thereafter manufactures or acquires.

19. A special master was appointed by the United States District Court for the Northern District of California pursuant to Section III, paragraph 2a of the decree, to obtain information and evidence relative to plaintiff's efforts under Section III, paragraph 2 thereof in selling its can-closing equipment and the available market for the sale and disposition of such equipment. The same special master was appointed pursuant to the corresponding portion of the decree in the *American Can* case. The two companies were each required to comply separately with their respective decrees; however, the special master submitted joint reports to the district court covering the two companies in compliance with the two decrees.

20. (a) Paragraph 5 of Section III of the Final Judgment provided in part as follows:

> A. The base price shall be ten (10) times the rental for the particular type and model of container closing machine which was in effect for the calendar year 1950. In the event that the weighted average depreciated cost of the particular type and model of container closing machine, on the effective date of this Judgment, is higher than the base price such weighted average depreciated cost shall be taken as the base price; but in no instance shall this latter base price be higher than the current factory cost of that type and model of container closing machine on the effective date of this Judgment.

Further provisions of this paragraph made adjustments in the "base price" by specified percentage discounts to take into account the time since the last reconditioning of the equipment, whether the lessee took the equipment "as is" and "where located," and for cash payment within ten days after sale.

(b) Paragraph 6 of said Section provided as follows:

> A. The maximum sales price of any related equipment owned by defendant on or prior to Jan-

uary 1, 1951, shall be computed in accordance with the provisions of paragraph 5 of this Section III. Where defendant had no established rentals in effect for the calendar year 1950 with respect to related equipment, the sales price thereof shall be reasonable, uniform and nondiscriminatory as provided for auxiliary equipment in Paragraph 6 B of this Section III.[1]

B. The sales price of any auxiliary equipment owned by defendant on or prior to January 1, 1951, shall be reasonable, uniform and nondiscriminatory. The terms and conditions of sale of auxiliary equipment shall be reasonable, uniform and nondiscriminatory.[2]

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[1] "Related equipment" was defined in Section I-D of the Final Judgment as follows:

"The term 'related equipment' means any integral machine manufactured or acquired by the defendant (other than container closing machines) which is used to supplement the operation of a container closing machine, or used in the preparing, filling or weighing of the contents prior to the final seaming, clinching, seating, or crimping of the metal of fiber covers, or in the unsealing, filling, and resealing of containers, or in the subsequent marking, identification, weighing, or handling of the closed container, including but not limited to key clinchers, spout clinchers and can opening machines."

[2] "Auxiliary equipment" was defined in Section I-E of the Final Judgment as follows:

"(1) Supplementary non-integral mechanisms manufactured or acquired by the defendant, which may be directly attached to container closing machines or related equipment to perform functions other than the double seaming, clinching, seating or crimping of metal or fiber covers to metal or fiber containers, including, but not limited to, can feeds, non-spill devices, take-away conveyors, discharge devices, but shall not include any particular special device made to one customer's specifications, and not manufactured thereafter.

"(2) Sets of change parts for container closing machines and related equipment manufactured or acquired by the defendant, and all other devices and equipment which will enable any container closing machine or related equipment to accommodate the containers of various types and sizes within the range of the particular container closing machine or related equipment."

21. The maximum selling price computed as hereinabove set forth (hereinafter referred to as the "decree price") at which the closing machines were to be sold, was substantially below the fair market value of the machines in 1951. The decree price was also below the manufacturing and replacement cost of the closing machines in 1951. For example, a so-called "Panama" model machine had a maximum decree sales price of $1,000. In 1950 the manufacturing cost of the same machine was between $3,000 and $4,000.

22. Container-closing machines and related equipment in the pre-1951 as well as post-1950 category were required to be made available in the order of priority as established by the decree. The lessee of any container-closing machines or related equipment on lease by plaintiff was given an absolute priority for the purchase of the leased machine or equipment. The lessee of any container-closing machine or related equipment was also given a priority to renew the lease on the leased equipment and for its replacement in the event of a major breakdown or destruction. Priorities for sales and leasing of container-closing machines and related equipment were thereafter to be granted in accordance with the chronological order in which written firm orders were received. Such applications for purchase or for lease were to be considered together.

23. Under the decree, plaintiff was ordered and directed upon application to afford to the employees of any applicant the opportunity to attend, without payment of tuition, the service training schools which plaintiff provided for the employees of its container customers for the purpose of educating them in the operation and repair of container-closing machines and related equipment sold or leased by plaintiff, during whatever period and on the same basis as plaintiff afforded such training courses to the employees of its container customers.

24. In carrying out its program of selling closing equipment, plaintiff made no changes in its sales organization. Sales of closing machines were made by plaintiff's regular container salesmen.

25. In complying with the decree, plaintiff developed a selling program for the sale of its container-closing equipment. Pursuant to this program, plaintiff furnished to all of its container-closing equipment lessees full and complete information as to the methods, terms, and advantages of purchasing and owning such equipment. This information, for the most part, was contained in advertising materials in the form of specially prepared letters and circulars.

26. Within sixty days of the date of the decree, plaintiff distributed to its container customers and lessees copies of the decree pursuant to Section VII thereof. Thereafter, plaintiff, in accordance with Section III, paragraph 7 of the decree, mailed a written notice to each person with whom plaintiff had a lease for closing equipment, informing such person of his right to purchase the equipment under the terms of the decree and quoting the base price for the types of machines which the person was then leasing from plaintiff.

27. After January 1, 1951, plaintiff, in compliance with Section III of the decree, granted each lessee of pre-1951 and post-1950 closing equipment an option to purchase such equipment.

28. The special master appointed by the court closely supervised the sales of closing machines by plaintiff and urged plaintiff to make greater efforts to sell. During 1951 the special master visited the offices of plaintiff regularly, at approximately monthly intervals, and made general audits of plaintiff's books to see that full compliance was being made with the terms of the antitrust decree.

29. In response to the urging of the special master, plaintiff prepared and mailed to lessees multicolored advertising folders describing the can-closing machines and the advantages of purchasing them at the decree price formulae. Excerpts from samples of this advertising material read as follows:

> (1) You'll save money * * * if you buy * * * not rent * * * Continental Closing Equipment.
>
> * * *
>
> Continental's previous commitments of guaranteed quality, discounts, credit terms (subject to credit approval), technical assistance and reasonable low cost service rates are still available on the same basis. We therefore urge you to consider without delay the purchase of your leased equipment.
>
> (2) As a businessman on the look-out for every possible economy—you will be interested in Continental's new plan for *buying* the closing equipment you now lease. It can mean many dollars to you.
>
> (3) We guarantee *buyers* the same highly skilled Continental service as *lessees!*

30. In response to the urging of the special master, in 1951 plaintiff offered a rental allowance to customers entitling them to credit a part of the rental paid against the purchase price of the machine.

31. During the year 1951, plaintiff had gross receipts from the sales of pre-1951 container-closing machinery and related equipment to lessees-in-possession in the amount of $4,005,899, and realized net gains from such sales in the amount of $1,720,639. These gains were reported on its federal income tax returns for the year 1951 as gains from the sale of capital assets held for more than six months. All of the aforesaid machinery and equipment was prop-

erty (a) used in plaintiff's trade or business, (b) of a character which was subject to an allowance for depreciation, and (c) held for more than six months prior to sale.

32. Although the decree did not establish a selling price for container-closing equipment manufactured or acquired by plaintiff after January 1, 1951, it did order plaintiff to sell to any applicant, for use, sale, or lease in the United States, as a condition to continuing the machine operations, any container-closing machine which it owned on the effective date of the provision, or thereafter manufactured or acquired. In addition, the decree provided for compulsory leasing of container-closing machines and related equipment in the following manner:

> Defendant is hereby ordered and directed, for a period of five (5) years from the effective date of this provision, to lease, upon written request, to any applicant * * * whether or not such applicant is a container customer of defendant, any container closing machine, and any related equipment or auxiliary equipment which it is then leasing to anyone, and which machine or equipment it has in stock or is currently manufacturing. Defendant shall not be required to manufacture for compulsory leasing hereunder any additional container closing machines, related equipment or auxiliary equipment requiring an aggregate expenditure of more than $1,000,000 in any calendar year. * * *

33. Closing machines manufactured or acquired by plaintiff in 1951, which were substantially identical with pre-1951 machines, were sold by plaintiff at much higher prices than the formula prices contained in the decree for pre-1951 equipment. The decree did not dictate the selling price of any can-closing machinery acquired or manufactured by plaintiff after January 1, 1951.

34. For the year 1951 plaintiff had gross sales of approximately $460,000,000, and of this amount approximately $370,000,000 represented sales of metal cans.

35. As part of its program for the sale of container-closing equipment, plaintiff's employees in the sales department became engaged in persistent personal sales efforts not only with lessees of plaintiff's equipment but also with other prospective purchasers.

36. The useful life of the container-closing machines, as agreed upon for depreciation deduction purposes, varied from 25 to 30 years.

37. Of the 1,708 container-closing machines sold to lessees-in-possession in 1951, at least 474 were acquired by plaintiff on or prior to 1925, of which at least 405 were acquired on or prior to 1920. Based on a computation taking 1920 as the earliest acquisition date, the average age of the machines sold would be 16.6 years. However, a substantial number of machines were acquired prior to 1920.

38. The sales of container-closing equipment to lessees-in-possession in 1951 were widespread rather than being confined to only a few of plaintiff's lessees.

39. Sales of container-closing machinery and related equipment occurred in the calendar year 1951 in at least four separate categories. These categories are as follows: (1) container-closing machines and related equipment acquired or manufactured by plaintiff on or prior to January 1, 1951, sold to lessees-in-possession of such machinery and equipment; (2) container-closing machinery and related equipment acquired or manufactured by plaintiff on or prior to January 1, 1951, sold to those who were not leasing the purchased machinery and equipment at the time of the sale; (3) container-closing machinery and related equipment acquired or manufactured by plaintiff after January 1, 1951, sold to lessees-in-possession of such machinery and

equipment; (4) container-closing machinery and related equipment acquired or manufactured by plaintiff after January 1, 1951, sold to those who were not leasing the purchased machinery and equipment at the time of the sale. Only the gains arising from the sales occurring in the first category are contended by plaintiff to be long-term capital gains. All others are concededly ordinary income and were treated as such.

40. The following schedule depicts plaintiff's business activities indicated with respect to container-closing machines and related equipment for the five-year period 1951-1955:

Year	*Gross rentals*	*Gross receipts from sales*
1951	$2,570,850	$4,245,298
1952	1,856,071	4,051,622
1953	1,795,966	4,178,083
1954	1,409,272	2,289,562
1955	1,529,336	889,637

41. Container-closing equipment identical with that manufactured or acquired by plaintiff prior to or on January 1, 1951, was manufactured or acquired by plaintiff after January 1, 1951, and from that date thereafter all such equipment generally was available for sale or rental by plaintiff.

42. With respect to the machines and equipment business, the decree required plaintiff:

> To maintain * * * for a period of ten (10) years complete and intact, in an orderly classification and available promptly on notice, permitting prompt and selective examination of particular documents or categories of documents, all its books, records, correspondence, memoranda, reports and other writings relating to its business of manufacturing, selling, and distributing container closing machines, related

equipment, auxiliary equipment, repair parts, and other equipment and the furnishing of machine services in connection therewith, or attempts to manufacture, sell and distribute container closing machines, related equipment, auxiliary equipment, repair parts and other equipment, and to furnish machine services in connection therewith.

43. The following table sets forth a five-year sales history of pre-1951 container-closing machines and related equipment and post-1950 container-closing machines and related equipment showing the percentage of gross receipts realized as net gains:

	1951	*1952*	*1953*	*1954*	*1955*
Gross Receipts from Sales of Pre-1951 Equipment	$4,229,848	$4,001,550	$3,704,835	$1,096,884	$735,046
Net Gains from Sales of Pre-1951 Equipment	1,835,506	1,805,272	1,213,127	721,993	314,860
Percentage of Gross Receipts Realized as Net Gains	39%	47%	33%	43%	43%
Gross Receipts from Sales of Post-1950 Equipment	15,450	50,066	473,248	592,678	154,591
Net Gains from Sales of Post-1950 Equipment	4,359	(588)	120,119	50,096	31,300
Percentage of Gross Receipts Realized as Net Gains	28%	.....	25%	8%	20%

44. On audit of plaintiff's return for the year 1951, the District Director of Internal Revenue, Upper Manhattan, New York, determined that the gain realized by plaintiff from the sale to lessees-in-possession of its container-closing equipment acquired on or prior to January 1, 1951, in the amount of $1,720,639, was ordinary income from the sale of property held by plaintiff primarily for sale to customers in the ordinary course of its trade or business, includable in plaintiff's gross income subject to ordinary income tax rates and to inclusion in plaintiff's excess profits net income.

45. On or about January 12, 1960, the District Director gave notice to plaintiff of an underpayment of income taxes of $960,476.59 and excess profits taxes of $1,425,670.24 for a total underpayment of $2,386,146.83. This alleged underpayment resulted from the aforesaid determination of the District Director.

46. On or about December 31, 1959, anticipating the notice of January 12, 1960, plaintiff paid to the District Director additional income and excess profits taxes of $678,984.22 for the calendar year 1951 and interest of $312,779.19.

47. On December 27, 1962, pursuant to the notice of January 12, 1960, and in accordance with a Waiver of Restrictions on Assessment and Collection of Deficiency in Tax and Acceptance of Overassessment (Form 870), dated December 27, 1962, plaintiff paid the District Director for the calendar year 1951 additional income and excess profits taxes of $1,949,357.23 plus interest thereon to said date of $1,261,180.72.

48. On July 12, 1963, plaintiff filed with the District Director of Internal Revenue, Upper Manhattan, New York, a claim for refund of income and excess profits taxes for the calendar year 1951, with the interest paid thereon, in the amount of $3,157,721, or in the alternative, for the recovery of federal excess profits taxes and interest paid thereon in the amount of $1,327,518.

49. More than six months had expired between the date that plaintiff filed the aforesaid claim for refund for the calendar year 1951 and the date that the petition in the instant proceeding was filed by plaintiff. On June 30, 1964, a notice of disallowance in full of said claim for refund was mailed by the Commissioner of Internal Revenue to plaintiff by certified mail.

50. No action on said claim for refund has been had or taken by the Congress or any of the departments of the

United States Government (other than the denial of plaintiff's claim for refund by the Internal Revenue Service) or in any other judicial proceedings.

51. During the years 1947 through 1950, plaintiff received income arising out of claims, awards, judgments or decrees as follows:

Description	*1947*	*1948*	*1949*	*1950*
State and Local Tax Refund and Interest	$1,818	$51,485	$10,433	$6,855
Bad Debt Recoveries	5,485	12,937	2,911	2,666
Other Claims (freight)	173	597	253	230
Total	7,476	65,019	13,597	9,751

During the year 1951 plaintiff received income from state and local tax refund and interest, bad debt recoveries, and other claims (freight) as follows:

Description	*Amount*
State and Local Tax Refund and Interest	$44,427
Bad Debt Recoveries	12,140
Other Claims (freight)	615
Total	57,182

Conclusion of Law

Upon the foregoing findings of fact and conclusions of law, which are adopted by the court and made a part of the judgment herein, the court concludes as a matter of law that plaintiff is not entitled to recover and the petition is dismissed.